

File

 Scott's *Restaurants Co. Limited*



Annual Report — December 26, 1971

Directors and Officers



DIRECTORS

GEORGE R. GARDINER

F. RONALD GRAHAM

WILLIAM J. BUSHNELL

ROBERT A. STEVENS

JOHN J. LEON

JOHN E. COLES

MRS. HELEN D. PHELAN

THE HON. SALTER A. HAYDEN, Q.C.

OFFICERS

GEORGE R. GARDINER

Chairman of the Board

F. RONALD GRAHAM

Vice-Chairman of the Board

JOHN J. LEON

President

JOHN E. COLES

Vice President

PETER J. M. BURGER

*Vice President; General Manager
Take-Out Operations — Ontario*

THOMAS W. CHASE

*Vice President; General Manager
Food Service Operations*

MELVILLE W. FANSHAW

*Vice President; General Manager
Take-Out Operations — Quebec*

JAMES G. GIBSON

Vice President; Finance and Treasurer

EDMUND V. GRAHAM

Secretary

Head Office

2000 Jane Street, Weston, Ontario

Solicitors

McCarthy & McCarthy

Registrars and Transfer Agents

Montreal Trust Company

Bankers

The Royal Bank of Canada

Auditors

Campbell, Lawless & Punchard

Listed

Toronto Stock Exchange

Montreal Stock Exchange

To Our Shareholders:

It is with great pleasure that I present to our shareholders the third annual report of Scott's Restaurants Co. Limited for the 52 weeks ended December 26, 1971.

- **1971 sales increased 27⁰/₀** to \$38,179,295 from \$30,023,495 in 1970.
- **1971 net earnings increased 41⁰/₀** to \$3,229,736 from \$2,290,013 in 1970.
- **1971 earnings per share increased 40⁰/₀** to 77³/₄¢ from 55¹/₂¢.

In November 1971 I had the pleasure of announcing the appointment of four members of our top management group to the position of Vice President in our Company. In addition to this we have instituted in-Company training programs covering all phases of our operations to assist employees in upgrading their capabilities. With continued expansion in mind, I feel that these steps are most important for the future of the Company.

While the past year was one of uncertainty in the business community it was gratifying to be able to maintain our rapid rate of growth throughout this period. It would appear that much of this uncertainty has now disappeared and is being reflected in our operations at the present time. Our program for the current year is for a continual rapid expansion of our Kentucky Fried Chicken Take-Outs.

The projected cash flow should provide the Capital funds necessary for this and other possible areas of expansion.

During 1971 our concentrated local advertising campaign on radio and T.V. has been most effective and our 1972 program calls for an even greater expansion in this form of advertising. In conjunction with this, your Company has materially benefited from the National Advertising of Colonel Sanders Kentucky Fried Chicken as it directs the travelling public to our familiar chicken take out facilities in Ontario and Quebec.

On behalf of the Board of Directors and Management I wish to express their appreciation to our 1950 employees for their able and loyal service and our thanks to the hundreds of suppliers who so ably take care of our needs.

On Behalf of the Board



J. J. Leon, President

April 7, 1972



In 1971 your Company opened an additional 12 Kentucky Fried Chicken Take-Out Shops, 5 in the Province of Ontario and 7 in the Province of Quebec, raising the Company's total to 115 Take-Out Shops. In the Province of Quebec our 37 Kentucky Fried Chicken Take-Out Shops operate under the name of Scott's "Villa du Poulet". In the Province of Ontario 78 locations operate under the name of Scott's "Chicken Villa".

In January of 1972 we opened 4 new outlets and have under construction at the present time 8 locations with 5 additional sites being finalized. For the year 1972, because of this excellent early start, we are forecasting 30 new openings.

Where a store by store comparison can be made between 1970 and 1971 it is interesting to note that the average sales per location have increased 20%.

In 1971 our commissaries processed over 10 million chickens and produced in excess of 4 million pounds of salad.

Our Highway Locations on the McDonald Cartier Freeway (401) enjoyed an excellent year showing increased sales and profits at all 7 Service Centres. We have also opened in co-operation with a major oil company a location off Highway 401 interchange at Lancaster, Ontario.

Scott's Restaurants Co. Limited

and subsidiary companies

Assets

	1971	1970
Current		
Cash and short term investments	\$ 1,698,456	\$ 1,476,548
Accounts receivable	116,676	143,086
Inventories at cost	320,884	275,876
Deposits and prepaid expenses	106,658	101,215
	2,242,674	1,996,725
Other		
Franchises, at cost less amortization	2,332,407	2,440,172
Fixed — at cost		
Land	1,995,557	1,405,618
Buildings	5,751,483	3,919,608
Equipment and motor vehicles	4,558,285	3,983,013
Leasehold improvements	1,337,381	1,221,192
	13,642,706	10,529,431
Less accumulated depreciation and amortization	2,414,463	1,984,576
	11,228,243	8,544,855
Goodwill purchased and excess of cost of investment in subsidiaries over values assigned to their net tangible assets	—	915,733
	<u>\$15,803,324</u>	<u>\$13,897,485</u>

Approved on behalf of the Board

George R. Gardiner, *Director*

J. J. Leon, *Director*

Consolidated Balance Sheet

December 26, 1971



Liabilities

	1971	1970
Current		
Accounts payable and accrued expenses	\$ 2,117,992	\$ 1,970,390
Current portion of long term debt	66,124	188,740
Income taxes payable	998,272	1,118,122
	<u>3,182,388</u>	<u>3,277,252</u>
Long-term debt	55,980	561,884
Deferred income taxes (note 2)	401,579	260,475
	<u>3,639,947</u>	<u>4,099,611</u>
SHAREHOLDERS' EQUITY		
Share Capital (notes 3 and 4)	5,648,606	5,597,106
Retained Earnings	6,514,771	4,200,768
	<u>12,163,377</u>	<u>9,797,874</u>
	<u>\$15,803,324</u>	<u>\$13,897,485</u>

Auditors' Report

To the Shareholders of Scott's Restaurants Co. Limited

We have examined the consolidated balance sheet of Scott's Restaurants Co. Limited and its subsidiaries as at December 26, 1971 and the consolidated statements of earnings, retained earnings and source and application of funds for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion these consolidated financial statements present fairly the financial position of the companies as at December 26, 1971 and the results of their operations and the source and application of their funds for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Toronto, Ontario
March 17, 1972

Campbell, Lawless & Punchard
Chartered Accountants

Consolidated Earnings

Year ended December 26, 1971

SCOTT'S RESTAURANTS CO. LIMITED
and subsidiary companies

	1971	1970
Sales	\$38,179,295	\$30,023,495
Cost of goods sold, operating and administrative expenses	31,604,805	25,210,198
Earnings from operations	6,574,490	4,813,297
Interest income	36,293	83,382
Earnings before income taxes	6,610,783	4,896,679
Provision for income tax — current	\$3,239,943	
— deferred (note 2)	141,104	
Net earnings for the year	\$ 3,229,736	\$ 2,290,013
Earnings per share (note 8)	\$.77 ³ / ₄	\$.55 ¹ / ₂

Consolidated Retained Earnings

Year ended December 26, 1971

	1971	1970
Balance at beginning of year	\$ 4,200,768	\$ 1,910,755
Net earnings for the year	3,229,736	2,290,013
	7,430,504	4,200,768
Deduct — goodwill purchased and excess of cost of investment in subsidiaries over values assigned to their net tangible assets	915,733	
Balance end of year	\$ 6,514,771	\$ 4,200,768

Consolidated Source and Application of Funds

Year ended December 26, 1971

SCOTT'S RESTAURANTS CO. LIMITED

and subsidiary companies



Source of Funds

	1971	1970
Net earnings	\$3,229,736	\$2,290,013
Add expenses included therein not requiring a current outlay of funds —		
Depreciation and amortization of improvements	737,977	524,127
Amortization of franchises	107,765	93,118
Deferred income tax	141,104	160,578
Shares issued in partial consideration for the purchase of subsidiary and franchises		200,000
Funds received from operations	4,216,582	3,267,836
Net increase in long term debt		302,044
Working capital of subsidiary at date of acquisition		60,797
Common shares issued for cash	51,500	12,500
Total of funds received	4,268,082	3,643,177

Application of Funds

Purchase of fixed assets	3,421,365	3,629,867
Cost of wholly owned subsidiary and related franchises expiring in 1994		450,000
Cost of other franchises expiring in 1994		1,050,000
Purchase of goodwill		178,975
Retirement of long term debt	505,904	
Other items		15,614
Total of funds expended	3,927,269	5,324,456
Increase (decrease) in working capital	\$ 340,813	(\$1,681,279)

Notes to the Consolidated Financial Statements

December 26, 1971

SCOTT'S RESTAURANTS CO. LIMITED

1. Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Scott's Restaurants Co. Limited and its subsidiaries, all wholly owned.

2. Income Taxes

The companies follow the tax allocation principle of providing for income taxes whereby deferred income taxes are set up with respect to capital cost allowances claimed for tax purposes in excess of depreciation recorded in the accounts.

3. Share Capital

Authorized

5,000,000 shares without par value

Issued

	Number of Shares	Dollars
Balance at December 27, 1970	4,143,260	\$5,597,106
Shares issued in connection with exercise of employee share options (note 4)	21,500	51,500
Balance at December 26, 1971	4,164,760	\$5,648,606

4. Employee Share Option Plans

The company has in force share option plans for certain of its employees under which options were taken up during the year to the extent of 15,000 shares at \$0.833 per share and 6,500 shares at \$6.00 per share. Options outstanding at the year-end were 15,000 exercisable at \$0.833 per share to June 30, 1973 and 13,500 exercisable at \$6.00 per share to September 12, 1974.

5. Long Term Leases

The company is committed in respect of rentals for a number of its properties requiring minimum rental payments of approximately \$270,000 annually to 1980.

6. Capital Commitments

The company and its subsidiaries were committed as at December 26, 1971 to capital expenditures of approximately \$332,000 in connection with their current expansion programme.

7. Remuneration of Directors and Officers

The aggregate direct remuneration paid by the companies to the nine directors as such was \$6,250 and to the seven officers was \$152,460.

8. Earnings per Share

The earnings per share figures are calculated using the weighted monthly average number of shares outstanding during the respective fiscal years (1971 — 4,153,843; 1970 — 4,130,760).

Combined Statement of Earnings

SIX YEARS

SCOTT'S RESTAURANTS CO. LIMITED

	FOR THE 52 WEEKS ENDING					
	December 26 1971	December 27 1970	December 28 1969	December 29 1968	December 30 1967	December 31 1966
Sales	\$38,179,295	\$30,023,495	\$18,810,516	\$11,882,891	\$9,295,392	\$6,863,291
Earnings before depreciation and amortization	7,420,232	5,430,542	3,160,152	1,852,596	1,197,937	701,065
Provision for depreciation and amortization of franchises	845,742	617,245	392,801	250,200	235,489	191,460
	6,574,490	4,813,297	2,767,351	1,602,396	962,448	509,605
Income from investments	36,293	83,382	81,473	—	14,172	11,137
Earnings before income tax	6,610,783	4,896,679	2,848,824	1,602,396	976,620	520,742
Income tax	3,381,047	2,606,666	1,511,701	839,634	499,853	265,315
Net earnings	\$ 3,229,736	\$ 2,290,013	\$ 1,337,123	\$ 762,762	\$ 476,767	\$ 255,427
Earnings per share	77 ³ / ₄ ¢	55 ¹ / ₂ ¢	38 ³ / ₄ ¢	24 ¹ / ₂ ¢	15 ¹ / ₂ ¢	8 ¹ / ₄ ¢
Number of Employees	1,950	1,875	1,525	992	792	791
Locations in operation	153	143	108	71	60	58

Outlets of Scott's Restaurants Co. Limited

SCOTT'S KENTUCKY FRIED CHICKEN TAKE OUTS

ONTARIO

Metropolitan Toronto

2000 Jane St., Weston
3765 Keele St., Downsview
1225 Danforth Ave., Toronto
851 Millwood Rd., Toronto
1638 Avenue Rd., Toronto
3351 Lawrence Ave. E., Scarboro
4755 Leslie St., Willowdale
6114 Yonge St., Willowdale
563 Gerrard St. E., Toronto
3495 Sheppard Ave. E., Scarboro
2567 Eglinton Ave. E., Scarboro
3719 Lakeshore Blvd. W., Long Branch
820 Kingston Rd., Toronto
1068 Coxwell Ave., Toronto
1760 Lawrence Ave. E., Toronto
2032 Kipling Ave. N., Rexdale
5322 Dundas St. W., Etobicoke
188 The Queensway, Toronto
1265 Lawrence Ave. W., Toronto
3810 Kingston Rd., Scarboro
829 St. Clair Ave. W., Toronto
3517 Dundas St. W., Toronto
2801 Kingston Rd., Scarboro
828 Dupont St., Toronto
1221 Dundas St. W., Toronto
11 Bloor Street W., Toronto
415 Mount Pleasant Rd., Toronto

Metropolitan Ottawa

1677 Bank St., Ottawa
942 Merivale Rd., Ottawa
932 St. Laurent Blvd., Ottawa
190 Dalhousie St., Ottawa
690 Bank St., Ottawa
1943 Baseline Rd., Ottawa
1096 Wellington St., Ottawa
Bells Corners — 3673 Richmond Rd.

Metropolitan Windsor

4449 Tecumseh Rd. E., Windsor
1916 Wyandotte St. W., Windsor
5869 Wyandotte St. E., Windsor
3006 Dougall Rd., Windsor
7435 Tecumseh Rd. E., Windsor
1797 Huron Line, Windsor
1747 Erie St. E., Windsor
Aurora — 130 Yonge St.
Belleville — 97 Station Rd.
Blenheim — 67 Talbot St.
Brampton — 42 Queen St. W.
Brantford — 53 Erie Ave.
— 79 Charing Cross St.

Chatham — 346 St. Clair St.
— 541 Queen St.
Clarkson — 1639 Lakeshore Rd. E.
Cobourg — 507 Division St.
Cooksville — 965 Dundas St. E.
— 1162 Dundas St. W.
Delhi — 7 King St.
Galt — 380 Dundas St.
Leamington — 277 Erie St. S.
Lindsay — 63 Lindsay St.
London — 1683 Dundas St. E.
— 37 Oxford St. W.
— 1072 Adelaide St.
— 689 Hamilton Rd.
Malton — 7161 Goreway Dr.
Oshawa — 474 Simcoe St. S.
— 973 Simcoe St. N.
Paris — R.R. #1
Peterboro — 786 Chemong Rd.
— 264 Water St.
— Highway #28

Richmond Hill — 191 Yonge St. N.
Rondeau Park
Simcoe — 472 Norfolk St.
St. Thomas — 973 Talbot St.
Trenton — 186 Front St.
Wallaceburg — 1239 Dufferin St.
Whitby — 301 Dundas St. W.

QUEBEC

Metropolitan Montreal

351 Regina St., Verdun
200 Taschereau Blvd., Greenfield Park
140 St. Foy Blvd., Longueill
8710 Sherbrooke St. E.
129 D'Anjou Blvd., Chateauguay
1670 de la Concorde Blvd., Duvernay Laval
2110 Henri-Bourassa Blvd. E., Montreal
1551 Shevchenko Blvd., Lasalle
1110 Provost St. Lachine
345 St. Martin Blvd., Chomedey-Laval
3000 St. Charles Blvd., Kirkland
5260 de Salaberry St., Montreal
9205 Lacordaire Blvd., St. Leonard
1551 Rue Beaubien, Montreal
8575 Pie IX, Montreal
100 Notre Dame St., Repentigny
4940 Des Sources Blvd., Pierrefonds
600 Henri Bourassa West, Montreal
3300 Masson St., Montreal
6625 Victoria Ave., Montreal
5255 Park Ave., Montreal
1595 Cote Vertu, St. Laurent
1580 Cure Labelle Blvd., Chomedey

Alma — 550 Collard St.
Cap de la Madeleine — 14 Fusey St.
Chicoutimi Nord — 466 Ste. Genevieve Blvd.
Drummondville — 1605 St. Joseph Blvd.
Gatineau — 258 Notre Dame St.
Hull — 347 St. Joseph Blvd.
Jonquiere — 340 Centenaire Blvd.
Pointe Gatineau — 52 Greber Blvd.
St. Hyacinthe — 2975 Laframboise St.
St. Jerome — 291 Des Laurentides Blvd.
Ste. Therese — 60 Labelle Blvd.
Sept. Isles — 602 Laure Ave.
Three Rivers — 1080 Des Recollets Blvd.
Valleyfield — 314 Larocque Road

RESTAURANTS

234 Bay St., Toronto
12 Victoria St., Toronto
5322 Dundas St. W., Etobicoke
134 Sparks St., Ottawa

HIGHWAY LOCATIONS

Highway 401

Texaco Service Centre — Port Hope
Texaco Service Centre — Kingston
Texaco Service Centre — Morrisburg
Texaco Service Centre — Mallorytown (North)
Texaco Service Centre — Mallorytown (South)
Texaco Service Centre — Woodstock
Supertest Service Centre — Tilbury

Trans Canada Highway

Highway No. 7 — Perth Ont.

TAKE FIVE LOCATIONS

40 Wynford Drive, Don Mills
45 St. Clair Ave. West, Toronto
Erb St., Waterloo
1262 Don Mills Rd., Don Mills
101 Duncan Mills Rd., Don Mills
6 Lansing Square, Willowdale

DAVEY JONES FISH & CHIPS

3351 Lawrence Avenue East, Scarboro
565 Gerrard Street East, Toronto
189 Yonge Street, North, Richmond Hill

INDUSTRIAL LOCATIONS

19 — Toronto and Ottawa



La Villa du Poulet — Province of Quebec



Chicken Villa — Province of Ontario

**SCOTT'S RESTAURANTS CO.
LIMITED**

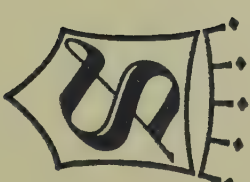
AND SUBSIDIARY COMPANIES

CONSOLIDATED BALANCE SHEET

AR49

Scott's Restaurants Co. Limited

	July 11, 1971 <i>(unaudited)</i>	Dec. 27, 1970 <i>(audited)</i>
Assets		
Current		
Cash.....	\$ 144,422	\$ 1,476,548
Accounts Receivable, Inventories and Miscellaneous.....	536,246	497,939
Franchise at cost less amortization.....	680,668	1,974,487
Mortgage.....	2,382,072	2,440,172
Fixed Assets at cost less depreciation.....	20,963	22,238
Excess of cost of investment in subsidiaries over values assigned to their net tangible assets.....	10,123,934	8,544,855
	915,733	915,733
	<u>\$14,123,370</u>	<u>\$13,897,485</u>
Liabilities		
Current		
Accounts payable and accrued expenses...	\$ 1,923,070	\$ 1,970,390
Current portion of long term debt.....	88,740	188,740
Income Tax Payable...	384,613	1,118,122
	<u>2,396,423</u>	<u>3,277,252</u>
Long Term Debt.....	116,473	561,884
Deferred Income Tax.....	302,649	260,475
	<u>2,815,545</u>	<u>4,099,611</u>
Shareholders' Equity		
Share Capital (4,161,510 shares at July 11, 1971).....	5,629,106	5,597,106
Retained earnings.....	5,678,719	4,200,768
	<u>11,307,825</u>	<u>9,797,874</u>
	<u>\$14,123,370</u>	<u>\$13,897,485</u>



**Interim Report
to Shareholders**

28 WEEKS ENDED JULY 11, 1971

August 30, 1971

Dear Shareholder

The unaudited statement of operations for the 28 week period ended July 11, 1971, shows sales of \$19,196,526, an increase of 31.4% over the same period in 1970. Profits after taxes for the same period were \$1,477,951, an increase of 37.6%.

The earnings per share for the 28 weeks ended July 11, 1971, were 35.5¢ compared to 26¢ for the same period in 1970.

Our continuing programme for opening new Scott's Kentucky Fried Chicken Take-Out Shops is proceeding satisfactorily. We have opened seven new locations in the past 28 week period; two in Toronto and five in the Province of Quebec.

Ten additional locations have been acquired and these are all expected to be in operation between now and December 31, 1971. Negotiations are in process for further locations, several of which will be in operation by the end of 1971.

We are confident that the balance of the year will show satisfactory growth in both sales and profits.

President

SCOTT'S RESTAURANTS CO. LIMITED
AND SUBSIDIARY COMPANIES
(unaudited interim report)

CONSOLIDATED STATEMENT OF EARNINGS

	<i>For the 28 weeks ended</i>	
	<i>July 11, 1971</i>	<i>July 12, 1970</i>
Sales.....	\$19,196,526	\$14,602,656
Earnings before depreciation and amortization.....	3,569,667	2,517,353
Provision for depreciation and amortization of franchises.....	446,286	291,588
Income from investments.....	3,123,381	2,225,765
Earnings before Income Tax.....	26,429	55,034
Income Tax.....	3,149,810	2,280,799
Net Earnings.....	1,671,859	1,206,976
	<u>\$ 1,477,951</u>	<u>\$ 1,073,823</u>

CONSOLIDATED STATEMENT OF SOURCE AND APPLICATION OF FUNDS

SOURCE OF FUNDS		
Net Profit for the period.....	\$ 1,477,951	\$ 1,073,823
Add Expenses not requiring cash expenditure including depreciation, amortizations and deferred income tax.....	488,460	327,838
Funds provided by operations.....	<u>1,966,411</u>	<u>1,401,661</u>
Proceeds from shares issued under employee option plan.....	32,000	12,500
Value of shares issued at market value as partial consideration for White Horse (London area) acquisition.....	—	200,000
Note issued on acquisition of White Horse.....	—	500,000
Other.....	<u>1,275</u>	<u>1,657</u>
	<u>\$ 1,999,686</u>	<u>\$ 2,115,818</u>
APPLICATION OF FUNDS		
Additions to Fixed Assets.....	1,967,265	2,024,728
Purchase of franchises expiring in 1994 and related goodwill for the operations in the London and Chatham areas.....	—	1,528,526
Reduction of Long Term Debt.....	<u>445,411</u>	<u>84,472</u>
	<u>2,412,676</u>	<u>3,637,726</u>
DECREASE IN WORKING CAPITAL.....		
Working Capital (deficiency) beginning of period.....	412,990	1,521,908
Working Capital (deficiency) end of period.....	<u>(1,302,765)</u>	<u>378,514</u>
	<u>\$ (1,715,755)</u>	<u>\$ (1,143,394)</u>

BONGARD LESLIE

INVESTMENT SECURITIES SINCE 1912

JANUARY 1971

AR49



institutional report

SCOTT'S RESTAURANT CO. LIMITED

Current Price	\$10 3/4	1970-71 high-low	\$11 3/4—7 1/8
Dividend	—	Yield	—
1970 Est. earnings/share	60¢	P/E multiple	17.9x
1971 Est. earnings/share	80¢	P/E multiple	13.4x
1972 Est. earnings/share	\$1.04	P/E multiple	10.3x

CAPITALIZATION AS AT DECEMBER 31, 1969

	<u>1969</u>	<u>%</u>
Long-Term Debt	\$ 185,472	2.4
Deferred Income Taxes	99,897	1.3
Minority Interest	7,779	0.1
Common Shares (4,108,260 outstanding*)	5,384,606	71.0
Retained Earnings	<u>1,910,755</u>	<u>25.2</u>
	7,588,509	100.0

Note: 1) Minimum annual rental commitments on long-term leases total \$218,000

2) 900,000 shares were sold to the public in September 1969 at \$6. About 75% of the total outstanding shares are held, primarily in trust accounts, by various directors and officers. There are no escrow restrictions on any of the shares.

CONCLUSIONS AND RECOMMENDATION

Scott's as a franchisee of Colonel Sanders Kentucky Fried Chicken is not subject to the problems—legal and accounting—which have been widely publicized in the franchise food industry. The shares of Scott's have been negatively affected as a result of an unclear understanding of the company.

Scott's, originally established as a food service company in 1937, is managed by a group of six individuals each having spent his career with Scott's in the food service industry. The length of service with Scott's ranges from 15 years to 33 years for each of the six operating senior management. Scott's is considered to be the best managed food service company in the industry.

With 1970 estimated sales of \$30 million from 102 company-owned retail outlets, and net profit of 60¢ per share, Scott's is one of the largest retail food services companies in Canada. Competition in the chicken takeout industry in Scott's market area is nominal, with no other chain holding a significant share of the market. The industry growth rate is at least 15% per year and Scott's has at best reached only 50% potential due to rising per capita consumption, lack of market penetration, and market growth rates.

Scott's has an enormous competitive advantage available to no other food takeout operation. The name and image of Colonel Sanders is probably the best known in the entire food industry in North America and is enjoyed by Scott's at a very insignificant cost. Other companies would require huge advertising expenditures to develop an equivalent product image.

Scott's reported a compound annual growth in sales of 37% in the five years from 1964 to 1969. In the year just ended the sales gain is estimated at 60%. In the same five years net profit increased at an average annual compound rate of 55% (fully taxed) and in 1970 the profit increase is estimated at 88% (on a per share basis the gain is 50% due to the issuance of shares to the public in 1969). The faster rate of gain in net profit, compared to sales, was due to major improvements in operating costs as materials, labour, advertising and other changes are spread over a larger sales base. In 1970, Scott's is anticipated to show a net margin of 8% up from 3.7% in 1966. A net margin level of 10% appears easily achievable in the medium term.

Internal cash flow is sufficient to finance 25 to 30 store openings per year, producing 10% to 12% new profit annually, together with 15% to 20% gains from existing outlets, to make a total of 30% profit increase, projected per year, exclusive of possible acquisitions.

Scott's has no significant long-term debt and is in a position to incur some form of long-term debt should new capital be required.

The shares at \$10 3/4, are currently selling at 18 times 1970 estimated earnings of 60¢ per share, and 13.4 times the current year earnings estimate of 80¢ per share. During 1971 it is anticipated that Scott's will trade at 20 times estimated 1971 earnings suggesting a price level of \$16, or, a capital gain of about 45% in less than one year. Investment in Scott's is recommended for short- and long-term capital gain potential.

FRANCHISE FOOD RESTAURANTS and SCOTT'S RESTAURANTS

Food franchising companies have recently undergone severe criticism, both from accounting and legal points of view, which has resulted in sharp declines in the shares of many public franchising companies. Scott's Restaurants has, on occasion, been mistakenly included as a franchising company and as such, overlooked to a degree by the investment community. Scott's is not a franchisor but a franchisee, having received free of charge the Colonel Sanders' license and franchise for most of the Province of Québec and most major metropolitan areas of Ontario. The revenues and profits of Scott's are derived from the retail sales of its chain of wholly-owned restaurants, not from franchising fees, commissions or overrides, etc., and as such, Scott's must be considered as a restaurant chain with an exclusive right in its market area to sell the exceptionally well-known and highly profitable Colonel Sanders Kentucky Fried Chicken.

BACKGROUND INFORMATION

The Company

The company was originally incorporated as Bowles Lunch Limited in 1937 and operated a small chain of restaurants under the Bowles name. In 1957 the name was changed to Scott's Restaurants Limited and subsequently in 1968 merged with an associated company — Scott's Catering Limited — to form the present company, Scott's Restaurants Co. Limited. In early 1969 the capitalization was re-organized to its present form and in September 1969, Scott's went public with the issue of 900,000 common shares at \$6 per share.

Management

The senior operating management of Scott's consists of six individuals all of whom have worked together in the company as a team for 15 years at least. The average age of the six is about 50.

The President of Scott's — Mr. J. J. Leon — joined the original Bowles Lunch in 1952, became general manager of Scott's Restaurants in 1964, President in 1965 and then President of the present company upon amalgamation in 1968.

Mr. J. E. Coles, Vice-President, has been with the organization since 1952. In 1964 he was appointed General Manager of Scott's Catering and became President in 1965. Since 1968 he has been Vice-President of the amalgamated company.

Mr. E. V. Graham, Assistant Secretary, has occupied his present position for five years and has been with the organization for 33 years.

Mr. T. Chase — Assistant to the President — has been with the organization since 1952.

Mr. P. Berger — General Manager, Ontario — joined Scott's in 1955.

Mr. M. Fanshaw — General Manager, Québec — has been with the company since 1932.

These six individuals have all spent the majority of their careers in the food service industry with Scott's and as a group, probably have a more extensive knowledge of the industry than the management of any other food service company in Canada.

Management policy is to work together, holding monthly meetings of the six. Each individual is expected to have a knowledge of each other member's function, sufficient that the jobs are interchangeable. Because of the extensive co-operation and team approach to management and the length of time the group has been together, an excellent rapport is evident among the individuals.

Operations

Originally, the company operated a group of restaurants catering to men only. In 1952, Scott's entered the industrial catering business and expanded its restaurant operations. In 1962, Mr. Leon was successful in obtaining a Kentucky Fried Chicken license and a program of store openings was launched. In 1963, Scott's opened its first Highway Service Centre restaurant together with Texaco. Presently the company is divided into three operating divisions; the Kentucky Fried Chicken Take-Out Shops, the Restaurant and Highway Service Centres, and Industrial Catering. Scott's is one of the five largest retail food service companies in Canada, with 1969 reported sales of \$18.8 million.

COLONEL SANDERS KENTUCKY FRIED CHICKEN FRANCHISE & SCOTT'S RESTAURANTS

The head company, which owns all the patents, rights, trademarks, recipes, etc., in Canada is *Col. Sanders Kentucky Fried Chicken Ltd.* (KFC). It is the licensor and has no connection whatever with the American company, Kentucky Fried Chicken Corp., with which Colonel H. Sanders was formerly associated. The Canadian company is a private company with Colonel H. Sanders as President, J. J. Leon — president of Scott's — as Vice-President, and E. V. Graham — Assistant Secretary of Scott's — as Assistant Treasurer. Mr. Leon, Mr. Graham and Colonel Sanders do not own any shares of KFC (all shares are held in trust) but perform executive functions for the company.

Kentucky Fried Chicken of Canada licenses are given to individual licensees such as Scott's for specific market areas and for a stipulated period of time. If a licensee later wishes to sell his outlets, he is required to obtain approval from KFC and a deal is negotiated, usually with another licensee.

The income of KFC is generated from each licensee. First, KFC receives 5¢ per chicken from each licensee, which accounts for the great majority of KFC income. In addition, each licensee buys equipment, spices, buckets and other paper supplies from KFC. The licensee orders all paper supplies directly from the manufacturer and is billed by KFC. With this method KFC receives better prices for volume orders. A mark-up of about 8% on buckets and 20% on paper supplies is charged to the licensee; however, if a licensee wishes he is free to order his paper and box supplies independently, but it is highly unlikely a licensee could match the price discounts available to KFC. All food supplies — chicken salads, drinks, etc. — are bought independently by licensees at the best prices obtainable.

Scott's is the largest licensee of Kentucky Fried Chicken. In the franchise agreement dated January 1, 1969, and expiring December 31, 1994, Scott's has been granted the exclusive license and franchise to all KFC patents and trademarks for the Province of Québec (except 13 locations), the whole of Metropolitan Toronto, Ottawa and district, Oshawa, Whitby, Brampton and Galt (except one location). Also, Scott's has exclusive rights on the Macdonald-Cartier Freeway (Highway 401) from Windsor to Montreal.

CHICKEN TAKE-OUT SHOPS

Beginning with Scott's first take-out shop in 1962, this division has shown remarkable growth to the point where it now accounts for about 80% of Scott's sales and profits. By 1968 there were 33 take-out shops in operation.

In 1969, 16 outlets were acquired from other franchisees and 19 were opened by Scott's, to make a total of 68 outlets. In 1970, 15 outlets were acquired and 19 opened to total 102 outlets.

Industry Growth and Competition

During the 1960s, fast-food and take-out restaurants emerged in Canada and exhibited a remarkable growth. Although statistics are not available, it is estimated by industry sources that this area of the retail food industry is currently growing at least 15% per year and has the potential to maintain this rate for many years to come. In the U.S., where the industry is in a more advanced state of maturity, a market of 10,000 people is considered sufficient to support one chicken take-out shop. In Canada, and especially in Scott's market areas, market penetration is not even close to this.

Within the fast-food industry, a distinction can be made between two types of outlets. The first, primarily hamburger shops, cater to customers who usually eat the food on the premises — either at seats in the shops, or in their cars in the parking lot. These outlets normally do a steady trade during the day and, as well, through the evening, especially later with the younger people. The second type of outlet could be more accurately termed a take-home operation with Scott's being the best example of this. Chicken, together with accompanying salads and beverages, is sold as a complete meal designed for families as well as individuals. Typically, most of the business is done at the supper hour and on the week-ends when a meal is purchased and taken home to eat. The prime difference being that it is a family type meal generally consumed at home.

Although Scott's and fast-food hamburger shops do not cater to the same specific market, there is likely an overlap of markets where some customers would patronize the most convenient take-out shop. Scott's, however, is quite prepared to locate an outlet close to other types of fast-food stores, feeling that their mutual markets are sufficiently exclusive.

Scott's, with 102 outlets, is the largest single chain in its market area. Direct competition from other chicken take-out restaurant chains is limited, totalling about 50 outlets divided among several small chains. As well, there are independent chicken take-out shops directly competitive with Scott's.

Scott's enjoys a major competitive advantage over all other chicken take-out chains because of the association with the Colonel Sanders Kentucky Fried Chicken name. Advertising in the U.S. has made Colonel Sanders' name and face the most well-known in the entire food industry. The spill-over into Canada has resulted in the Colonel and the product being equally well-known here and at an insignificant cost to licensees. An additional benefit is that any visitor from any KFC market area in Canada and the U.S. will likely know the Colonel Sanders product.

FOOD SERVICES

This division is comprised of five restaurants, industrial catering services, Take-Five Shops, and vending operations and is estimated to contribute 5% to 7% to overall company sales and profits. Four of the restaurants have liquor licenses and seating capacities vary from 50 to 160 customers. Sales and profit growth is considered satisfactory. Industrial catering services consist primarily of in-plant feeding. The operation is subject to a high labour content and low profit margins and consequently, Scott's does not anticipate significant growth in this area. Vending machine operations are considered to be steady, with satisfactory profit margins. The Take-Five Shops are a recent innovation, small restaurants offering sandwiches, salads, and beverages. Capital investment and labour requirements are low while profits are good. Currently, Scott's has six Take-Five Shops in operation, all owned, and expects to gradually expand the number of outlets.

HIGHWAY SERVICES DIVISION

Under its exclusive license agreement with KFC, Scott's manages seven restaurants on the Macdonald-Cartier Freeway (Highway 401) on leased premises from the major oil companies. Total profits from this area account for approximately 5% of Scott's overall net profit and growth is about 10% per year. In addition, Scott's, together with Texaco, is actively considering opening restaurants on the Trans-Canada Highway.

A new concept has been initiated — Davey Jones Fish & Chips. Scott's receives a royalty of 5% of sales of the Davey Jones Shops which are licensed by individuals. So far, three outlets are in operation and 10 additional licenses have been sold. This operation is expected to be small but with steady growth in profits.

ANALYSIS OF INCOME STATEMENTS

Following is an historical summary of Scott's income statement together with selected comparative ratios.

(\$000's) year-end December 31	Annual Financial Summary (Year end December 31)				
	<u>1965</u>	<u>1966</u>	<u>1967</u>	<u>1968</u>	<u>1969</u>
Sales	5,181	6,863	9,295	11,883	18,811
Operating Profit	570	701	1,198	1,853	3,186
Other Income	30	11	14	—	56
Depreciation	138	191	235	250	393
Profit Before Taxes	462	521	977	1,603	2,849
Provision for Taxes	221	265	500	840	1,512
Net Profit	241	256	477	763	1,337

Financial Statistics

Number of KFC Outlets				33	68
Sales — % Change	+15.2	+32.5	+35.4	+27.8	+58.3
Operating Profit — % chg.	+54.4	+23.0	+70.9	+54.7	+71.9
Operating Profit Margin — %	11.0	10.2	12.9	15.6	16.9
Tax Rate — %	47.8	50.9	51.1	52.4	53.1
Net Profit — % Change	+58.5	+ 6.2	+86.3	+60.0	+75.2
Net Profit Margin — %	4.7	3.7	5.1	6.4	7.1

Five-Year annual compound growth 1964-69 — Sales + 37%; Net Profit +55%.

SALES

Sales revenue increased at an annual compound rate of 37% in the five years 1964 to 1969, and increased by 58.3% to \$18.8 million in 1969. (During the five years, no price increase has been implemented at any Scott's outlet.) The KFC outlets are estimated to account for at least 80% of total company sales while the Food Services and Highway Services divisions make up the remaining 20%.

The major growth in sales comes from the KFC take-out division with the other two providing moderate annual gains — 10% per year sales increase at best.

Scott's phenomenal growth in sales was from three sources — acquisitions of existing KFC outlets from other licensees, new store openings, and internal growth. Until 1968, acquisition was not a major factor in company growth but with re-organization and restructuring of the capitalization in 1968, Scott's was in a position to purchase KFC outlets from other licensees. In 1969 and 1970, thirty-one outlets were acquired and integrated into the Scott's operation. In the same period 1969-1970, thirty-eight Scott's KFC outlets have been opened, to make the present total of 102 Scott's KFC outlets. Internal sales growth of existing outlets is estimated by Scott's management to increase at an average of 20% per year without any price increase, reflecting the high growth rate of the chicken take-out industry, estimated at 15% to 20% per year and, as well, the success of management in choosing locations and promoting the product.

OPERATING COSTS

Operating profit margins, reflecting operating costs, have shown major improvement in the last five years, reaching 16.9% in 1969 from a low of 10.2% in 1966. A major reason for this excellent performance is that Scott's, as the owner of its outlets, manages all the operating aspects of each store, receiving the direct benefits of volume purchasing and control of labour and other expenses.

Chickens are purchased from Ontario and other processors at an average price of 41¢ per 2 1/4 to 2 1/2 lb. chicken. Under the auspices of the Ontario Poultry Marketing Board. On occasion when Ontario supply is limited, the company purchases birds from Québec where the price is generally cheaper. Chicken prices in both provinces have remained generally stable with no price increases. Recently, there has been discussion of implementing regulations to require Ontario buyers to purchase Ontario-produced chickens. If this occurs, Scott's, as probably the largest single purchaser of chickens in Ontario (26% of Ontario production), would still receive the best prices because of volume considerations, and also the price spread between Ontario-produced and Québec chickens is nominal, indicating no significant cost increase is likely. Scott's is estimated to have spent \$1.3 million in 1970 for chickens.

Chickens are delivered to Scott's centrally located commissaries where they are cut to specification then delivered fresh (not frozen) to Scott's outlets, together with batter, salads, etc.

No cost estimate of paper supplies is available or total value of royalties paid by Scott's to KFC.

Labour

Scott's outlets are all managed by employees, not independents. In an average store grossing about \$300,000, the manager received about \$7,500 per year, the cook \$6,000 to \$7,000, plus part-time help paid on an hourly basis. In total, direct store labour costs would total about \$30,000 annually, or 10% of the annual gross of the outlet. In addition to the afore-mentioned direct store labour costs, supervisory staff is likely to receive a total of about \$100,000 annually. Five commissaries, employing about 35 men plus about 5 truck drivers, service the stores with fresh products. The labour bill for this is estimated at \$300,000 per year.

Other labour costs include administrative and corporate staff, estimated at \$140,000 per year, and officers' and directors' remuneration of \$131,354. Although it is difficult to estimate accurately, Scott's labour bill is likely in the range of about \$3.7 to \$4 million in the current year, equal to about 14% of gross sales.

Advertising

KFC licensees set up a board to manage national advertising of the product. Each licensee contributes 2¢ per chicken bought plus KFC turns over one cent per chicken from the 5¢ per chicken received from all licensees. These funds are then used for national advertising under the auspices of a General Manager in charge of advertising. National advertising costs to Scott's are nominal, totalling an estimated \$75,000 on sales of \$30 million in 1970.

In addition to Scott's share of national advertising, the company is estimated to have spent around \$750,000 in 1970 on regional advertising of its products. This is done primarily on radio. In total, Scott's advertising bill this year approximates \$825,000, or about 3% of gross revenues. As previously mentioned, the spill-over of U.S. advertising, plus the extensive publicity which Colonel Sanders receives, provides enormous advertising benefits to Scott's at no cost.

The available information is insufficient to accurately break out all factors involved and develop a complete estimate of costs, so it is necessary to rely on the historical trend of overall operating profit margins. These, as mentioned, have shown an outstanding improvement. In comparison with other fast food take-out chains — those which derive sales and profits from the retail sales of the outlets rather than those deriving income from franchise fees, royalties, etc.— Scott's ranks extremely well, with a 1969 operating profit margin of 16.9%.

In assessing the stability of individual costs of operation, Scott's is not subject to undue risk in that cost of materials and paper supplies are not subject to volatile price swings and, as evidenced by the profit margins, are easily absorbed by Scott's. Labour is not particularly high-skilled and is plentiful, indicating labour costs will not rise excessively. Advertising expenditures are a very small, estimated 3%, of gross sales. Rental charges (to be discussed more fully later) are all long-term leases without override clauses or percentage increases based on sales.

As volume of sales increases and new acquisitions become fully efficient, the operating profit margin is expected to expand. For example, currently there are five commissaries servicing 102 retail outlets but the optimum ratio could be one commissary for 35 outlets with only moderate additions to staff. Another major increase in efficiency occurs when a group of KFC outlets is acquired. Generally, an independent group will pay high salaries to the owner, plus one or two others in management and, as well, will have an office staff to administrate the group. When acquired by Scott's, a salaried manager is appointed to run each store and all administration is absorbed by Scott's head office with no significant increase in office administration. Also, savings result on purchase of materials due to Scott's high volume. The result is that after acquisition it is not unusual for the profits of the acquired group of outlets to double, and Scott's operating margin to expand.

DEPRECIATION

In the early years of Scott's development of KFC outlets, the company controlled each location, owning the land and buildings as new outlets were opened. Attendant depreciation charges rose quickly — 38% in 1966 — which accounted for the only year in which the net profit margin decreased. In 1967, depreciation increased 23% and margins resumed their upward trend. The capital investment required to open new KFC outlets varies from \$100,000 to \$225,000, depending on the cost of land. At these rates, cash flow (the major source of funds available for expansion) would only support three to five store openings per year, not sufficient to capitalize on market opportunities.

In 1968, in order to release capital for major expansion, Scott's sold all its land and buildings in Québec and Ontario to Bowles Enterprises (1968) Limited, a private company controlled by some of the officers and directors of Scott's for a cash consideration of \$1.465 million. The properties were then leased back to Scott's on leases expiring May 20, 1978 (renewable at Scott's option for a further 10 years). Also in 1969, Scott's became a public company raising \$5.4 million with a public issue of shares. The proceeds of the two transactions totalled \$6.865 million, which was used to open new KFC outlets and acquire other KFC licensees.

After 1967, depreciation charges increased at a lower rate proportionate to sales and profit gains and the internal cash flow generated increased substantially as a result of the major expansion. Currently, cash flow (estimated at least \$3.0 million in 1971) enables Scott's to internally finance 25-30 new outlets, assuming a significant number do not require a full \$225,000 investment in land and buildings.

INCOME TAXES

Scott's tax rate has been between 50% and 53% of earnings for the last several years. The company follows the normalized method of tax accounting, reporting deferred taxes charged in 1969 at \$80,161 of a total income tax charge of \$1.5 million. Accumulated deferred taxes equalled \$99,987 in 1969.

NET PROFIT

Net profit increased at an annual compound rate of 55% during the five years 1964 to 1969 and the increase in net was 75.2% in 1969. Two major acquisitions were made which contributed to the profit gain.

Fosters, operating eight KFC outlets, was acquired as of July 1969, and Windovers, also with eight KFC outlets, was acquired effective the last quarter of 1969. Together, they are estimated to have contributed about 5% to Scott's 1969 reported sales and earnings gains. The rest resulted from internal growth and 19 new store openings.

The annual gains in profits have consistently outpaced the sales increases, indicating major improvements in efficiency. The net profit margin increased to 7.1% in 1969 from 6.4% in 1968 and a low of 3.7% in 1966. As the sales base gets larger, major improvement in the profit margin is anticipated since commissary, administrative, labour, advertising and depreciation charges are spread over a larger sales base. The minimum anticipated overall sales growth per year is 30%, (10% to 12% per year from new store openings and 15% to 20% at least from internal growth), exclusive of acquisitions. None of the major charges against income is likely to increase at this rate, resulting obviously in increasing profit margins.

1970 EARNINGS

To date, Scott's has reported earnings for the first 3 quarters of fiscal 1970:

Consolidated Statement of Operations

	For the 40 Weeks ending.....	
	October 5, 1969	October 4, 1970
Sales	\$13,782,723	\$22,854,786
Profit Before Tax	1,996,674	3,845,949
Provision for Taxes	1,055,969	2,043,667
Net Profit	\$ 940,705	\$ 1,802,282
E.P.S.	22.9¢	43.9¢
Net Profit Margin	6.8%	7.9%
Tax Rate	52.9%	53.1%

The profit increase of 91.6% in the first nine months of 1970 substantially outpaced the sales gain of 65.8% and both are much higher than the average annual gains in sales and earnings during the last five years. Net profit margin was much higher at 7.9% than the 6.8% for the comparable period in 1969 and also much higher than any other year. This is a result of greatly improved efficiency.

The 1970 results to date include the results of the 16 outlets acquired in late 1969 and two other acquisitions in 1970. The first, in January 1970, was the Seeger group of six outlets, and the second, the Whitehorse group of ten outlets acquired in May. In total, the contribution to 1970 results is estimated at 10% of sales and earnings. Other major sources of sales and earnings gains in the 1970 were the group of 19 new outlets opened during 1969, which operated for all of the current year and the opening of 19 new outlets during the course of 1970. The remainder of the growth resulted from internal growth of existing outlets together with substantially better profit margins.

In the fourth quarter of 1969, company sales were \$5 million and net profit was \$396,000. The remaining quarter of 1970 will have the contribution to sales and profits of the 16 outlets acquired during the year, plus the new outlets. As well, Scott's will benefit from the increased profit margins as new outlets develop optimum revenues and good growth in existing outlets. Last quarter sales are estimated to have increased at least 40% and earnings by at least 50% to make total 1970 estimated sales of \$30 million and net profit of about \$2.5 million, equal to approximately 60¢ per share.

FUTURE

1971 earnings growth and after depends on four major factors — 1) growth in sales and profits of existing outlets; 2) better profit margins; 3) new store openings; 4) acquisitions. To a lesser extent, Scott's growth will also be dependent on the Highway Services Division, Industrial Services Division and new concept stores such as the Take-Five Shops and the Davey Jones Fish and Chip stores. However, the KFC chicken take-out stores will account for at least 80% to 85% of company operations in the foreseeable future.

1) As has been discussed previously, the overall internal growth rate in sales and profits of existing outlets is at least 15% per year.

2) In the current year, the net profit margin should exceed 8% and as the sales base enlarges and the many new or acquired KFC outlets develop, optimum sales and profit levels, the net margin will expand. A major possible method to improve profit margins is to increase retail prices. This has not been done in five years but it is always possible. A 20% increase could be easily implemented. Scott's has the potential overall to increase profit margins above the 10% level in the next few years.

3) Current internal cash flow enables Scott's to open 25-30 new stores per year. As time goes on, the cash flow will expand, enabling the company to open more than 30 per year. Recently, Scott's opened a new concept KFC outlet — a small store on a main city street with limited parking. The idea behind this store is that it is a rented location not requiring large investment in land and buildings such as on a major highway or suburban artery. The high-density of population in the area will provide sufficient pedestrian traffic, together with some parking facilities, to provide good store traffic. The store, at Dupont and Shaw Streets in Toronto, has been very successful in its first two months' operation and is projected to gross \$350,000 revenue in its first year. The success of this take-out store suggests that KFC outlets can be successful in downtown or high-density population areas throughout the city, and opens up a very large potential market in Toronto and Montreal, which is to date relatively untapped.

4) Acquisitions — Successful acquisitions in the future depend on two basic factors — availability of other KFC outlets in Canada and sufficient capital to acquire groups. Scott's currently has 102 of about 375 KFC outlets in Canada, and is the largest licensee. This represents a large potential source of acquisition. Because of the unique relationship in which Scott's management also manage Kentucky Fried Chicken of Canada — the franchisor company — Scott's has complete information on the sales, costs, etc., of every KFC outlet and is in a position to have first chance at making an offer to a group while knowing exactly how well each outlet is doing. At this time, Scott's does not have the necessary capital to make a major acquisition without hampering its own program of store openings. However, Scott's, until now, has not used any bank lines of credit and carries almost no long-term debt (there is a mortgage payable of \$185,472), thus indicating the company would have no problem raising substantial capital if required. It would be considered very beneficial to incur bank debt or long-term to date in order to make acquisitions.

Earnings per Share

In 1971, Earnings per share are anticipated to increase 10% to 12% from new store openings and 15% to 20% from existing outlets, based on internal growth and improved profit margins. The earnings per share estimate for 1971 is a 30% increase to 80¢ compared with an estimated 60¢ in 1970. In 1972, a 15% to 20% earnings gain from existing outlets (including the new ones opened in 1970 and 1971) and 10% to 12% from 1971 store openings, would result in \$1.04 per share. Acquisitions would increase the earnings estimates for 1971 and 1972.

In percentage terms, Scott's is considered likely to increase earnings 30% per year minimum for the foreseeable future, exclusive of acquisitions. Acquisitions would increase this performance.

SUMMARY

Some important factors emerge from an analysis of Scott's which are instrumental in evaluating the company.

First, and most important, Scott's is not a franchisor and therefore not subject to the many problems recently besetting franchise operations. These include the necessity of buying back franchises, and management problems when experienced food retailing people are not in control. Scott's is a franchisee having received an exclusive license in its area to market the highly successful Colonel Sanders Kentucky Fried Chicken products. The major decline in the shares of several franchisors recently has likely affected the price of Scott's shares because of this lack of understanding of Scott's.

Scott's has the potential to report major increases in sales and profits for the foreseeable future based on its unique position in Canada, the industry growth rate, and proven management abilities. Profit margins can show major improvement based on the afore-mentioned efficiencies as the sales base expands and if the company chooses to raise the price of its products. A minimum of 30% increase per year in sales and earnings is anticipated for the foreseeable future, exclusive of acquisitions.

MEMORANDUM

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MEMORANDUM

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